



Trusts

WRITTEN BY ASHLEY STAUNTON

Trusts – How Do They Work?

- Trusts must distribute income to beneficiaries each year in accordance with their trust deed
- Unlike companies, a trust will not hold retained earnings at the end of a year (other than in exceptional circumstances)

Trusts – Types of Trust

Trusts fall into two categories

- Fixed Trusts
- Discretionary Trusts

Trusts – Fixed Trusts

- The percentage of distribution to each beneficiary is fixed each year
- Most common type of fixed trust is a unit trust
- In a unit trust the percentage of distribution is determined by the number of units held by each beneficiary

Trusts – Discretionary Trusts

- The distributions are variable each year
- The beneficiaries of the trust are listed in the trust deed
- The trustee has the discretion to appoint distributions to the various beneficiaries in whatever percentages they see fit – as long as it is allowed by the trust deed
- The trustee can exclude beneficiaries from distributions – as long as it is allowed by the trust deed

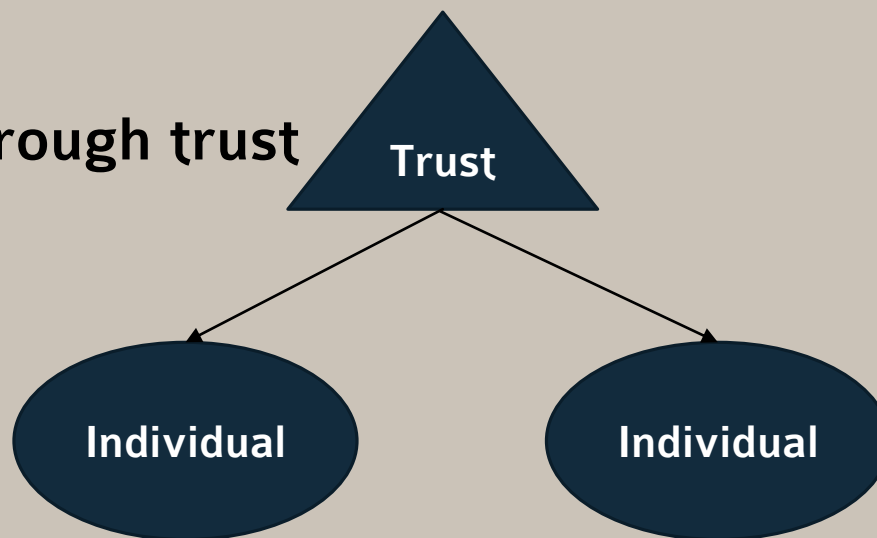
Trusts – What Are The Advantages And Disadvantages

Advantages	Disadvantages
<ul style="list-style-type: none">• Flexibility of tax distribution	<ul style="list-style-type: none">• Complexity of rules<ul style="list-style-type: none">i. Trust lossii. Division 7A distributionsiii. CGT Small Business Concessions
<ul style="list-style-type: none">• Estate planning benefits	<ul style="list-style-type: none">• Requires a trustee
<ul style="list-style-type: none">• Capital Gains Tax 50% Discount	<ul style="list-style-type: none">• Limited ability to distribute to children until their 18yo
<ul style="list-style-type: none">• Asset protection	<ul style="list-style-type: none">• Tax losses quarantined
	<ul style="list-style-type: none">• Not generally recognised for Gov't grants

Trusts – Common Structures

Business operated through trust

Profits distributed
to individuals

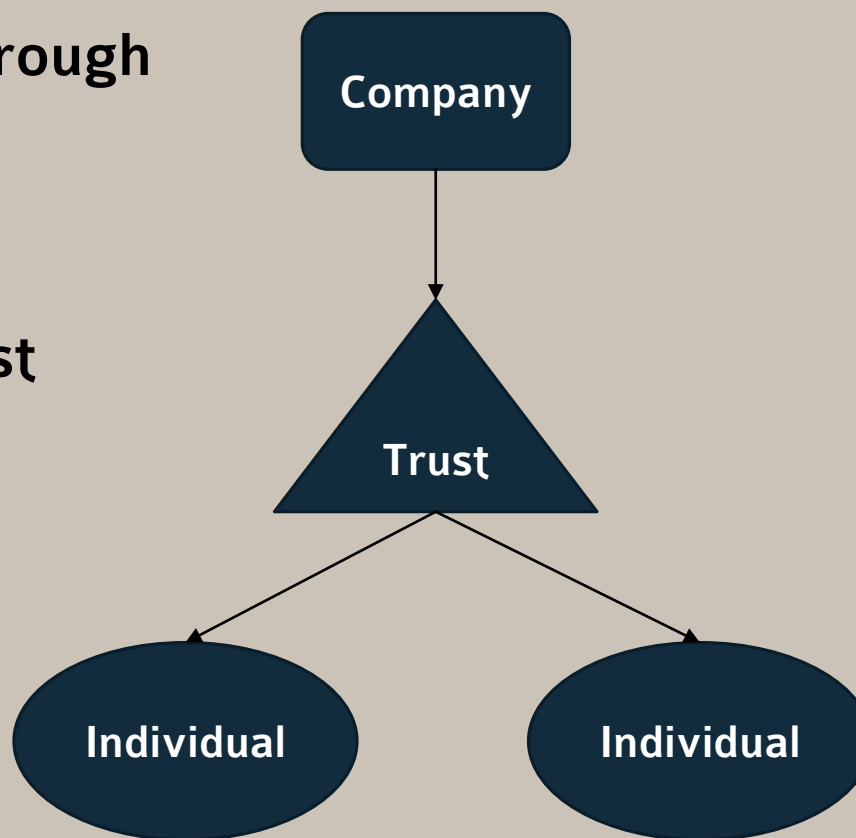


Trusts – Common Structures

Business operated through company

Dividends paid to trust

Trust distributes to individuals

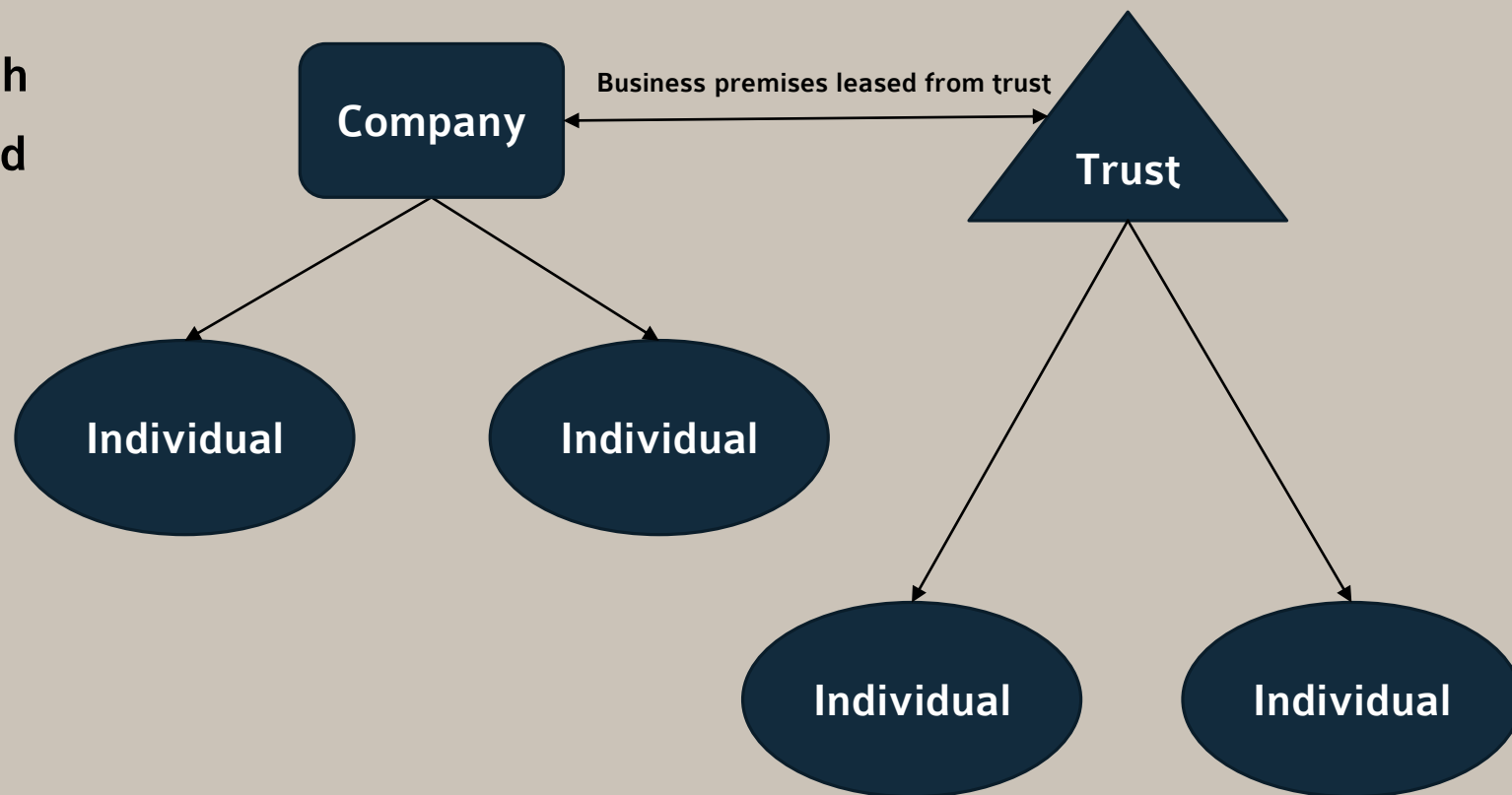


Trusts – Common Structures

Business operated through company, premises owned by trust

Dividends paid to individuals

Rental profits distributed to individuals



Trust – Accounting For Trusts

There are some book entries that are unique to trusts

- Entries to record equity contributions
- Entries to record annual distributions

Trusts – Recording Equity

- Trust equity takes the form of
 - ◆ Contributions by the settlor (discretionary trust)
 - ◆ Contributions by the unitholders (unit trust)
- The book entries to record equity are made on settlement and there are often no further entries to these accounts for the life of the trust
- The equity contributions are often only for nominal amounts ie: \$10 settled sum or units at \$1 each

Trusts – Recording Equity

The entries to take up trust equity will usually look like this:

Account	DR	CR
Cash on hand	\$10	
Settled sum		\$10

Or, if a unit trust:

Account	DR	CR
Cash on hand	\$10	
Units issued		\$10

Trusts – Recording Distributions

- Most accounting software programs will close off profit to the retained earnings account at the end of a financial year
- However, generally there are no retained earnings for trusts
- All profit is to be distributed to beneficiaries (paper distribution)
- Journal entries required to record the distribution and avoid retained earnings

Trusts – Recording Distributions

Using the following scenario as the basis for our example:

- Discretionary trust with profit of \$10,000 at year-end
- Two beneficiaries – John Smith and Jane Smith
- Trustee decides to distribute 50% of profit to John and 50% to Jane

Trusts – Recording Distributions

- Need to create the necessary accounts before entering distribution journal
- To use MYOB as an example, we would require the following accounts:
 - A distribution expense account for each beneficiary called “Distribution John Smith” and “Distribution Jane Smith”. Set up as “Other Expense” account types. Use account codes 9-9100 and 9-9200.
 - A liability account for distributions made but not yet paid called “Beneficiary Entitlement John Smith” and “Beneficiary Entitlement Jane Smith”. Set up as “Liability” account types. Use account codes 2-9100 and 2-9200.

Trusts – Recording Distributions

The journal entry to record the distribution at 30 June would look like this:

Account Number	Account Name	DR	CR
9-9100	Distribution John Smith	\$5,000	
2-9100	Beneficiary Entitlement John Smith		\$5,000
9-9200	Distribution Jane Smith	\$5,000	
2-9200	Beneficiary Entitlement Jane Smith		\$5,000

Trusts – Recording Distributions

Further journal entries would be required to record actual cash payments to the beneficiaries which would look like this:

Account Number	Account Name	DR	CR
2-9100	Beneficiary Entitlement John Smith	\$5,000	
2-9200	Beneficiary Entitlement Jane Smith	\$5,000	
1-1000	Cash at Bank		\$10,000

From a practical perspective this entry would be made using the “spend money” function in the accounting software.

Trusts - Summary

- Many reasons why a client may use a trust in their structure
- Client should speak with accountant before doing so
- Unique aspects of accounting for trusts are not overly complicated
- The accountant will usually advise the amount of the distribution entries to be made at year end, particularly for discretionary trusts